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**In the Supreme Court of the United States**

October Term, 1943 - - - - - Number 621

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**MINNESOTA MINING & MANUFACTURING COM-  
PANY,**

*Appellant,*

**vs.**

**WISCONSIN DEPARTMENT OF TAXATION,**

*Appellee.*

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**Brief of Minnesota Mining & Manufacturing  
Company, Appellant.**

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**I.**

**The Opinions of the Court Below.**

The opinion in the Supreme Court of Wisconsin filed June 16, 1943 is reported in 243 Wis. 211, 10 N. W. (2d) 174. It is also printed in the record at Page-102. The opinion of the same Court denying motion for rehearing filed September 14, 1943, is not yet officially reported but is reported in

11 N. W. (2d) 96. It is also printed in the record at Page 106.

An opinion in the companion case of *International Harvester Company vs. Wisconsin Department of Taxation*, which was adopted by way of reference in the decision of Wisconsin Supreme Court in the instant case is reported in 243 Wis. 198, 10 N. W. (2d) 169.

## II.

### Jurisdiction.

1. The jurisdiction of this Court is invoked under the provisions of Section 237(a) of the Federal Judicial Code (28 U. S. C. A. 344 (a)). Appellant further relies on Rule 46, Paragraph 2 of the rules of this Court.

2. The petition for allowance of an appeal was made to review the judgment of the Supreme Court of the State of Wisconsin in the instant case, and with such petition there was filed appellant's "Statement as to Jurisdiction" as required by the rules of this Court. The appellee moved to dismiss the appeal or in the alternative to affirm for the want of a substantial Federal question and filed its "Statement Opposing Jurisdiction". The appellant filed a brief opposing appellee's motion. On February 28, 1944 this Court noted "Probable Jurisdiction."

3. The appellant seeks review of the judgment of the Supreme Court of the State of Wisconsin upon appeal to it with respect to the validity as applied to appellant of Section 3 of Chapter 505, Laws of Wisconsin, 1935, as amended by Chapter 552, Laws of Wisconsin, 1935, and subsequent acts amendatory thereto, and tax assessments levied against appellant under such laws. The appellant throughout the proceedings has challenged the validity of the law as applied to it, and the assessments of tax levied against it.

contending that the law as applied in assessments against the appellant imposes a tax beyond the taxing jurisdiction of the State of Wisconsin, and therefore that the imposition of the tax as against the appellant by the assessments involved, constitutes a deprivation of the property of appellant and its stockholders without due process of law contrary to the provisions of the Fourteenth Amendment to the Constitution of the United States. The appellant further throughout these proceedings has contended in the alternative and does now contend that the assessments as made result in the imposition of a vulnerably retroactive tax and as such constitute a deprivation of appellant's property without due process of law under the Fourteenth Amendment. The Supreme Court of the State of Wisconsin denied relief to appellant on both constitutional questions,—although on the retroactivity phase the determination was by an evenly divided Court, resulting in affirmance of the lower court's determination in favor of constitutionality. No procedural questions are involved on this appeal.

4. Reference is also made to appellant's Statement as Jurisdiction and Brief of Appellant Opposing Appellee's Motion to Dismiss Appeal for a more comprehensive jurisdictional statement.

### III.

#### Statement of the Case.

This case involves the validity of certain assessments made against the appellant, Minnesota Mining & Manufacturing Company, a Delaware corporation, for so-called Wisconsin privilege dividend taxes pursuant to Section 3 Chapter 505 of the Laws of 1935 as amended and as extended by Chapter 309, Session Laws of 1937, and Chapter

198, Session Laws of 1939. This law is printed as an appendix to this brief.

The controversy at issue arose out of three separate assessments of so-called Wisconsin privilege dividend taxes under the laws above set forth.

In substance this law attempts to impose a tax of two and one-half per cent ( $2\frac{1}{2}\%$ ) (three per cent (3%) after July 1, 1939) on the amount of dividends declared and paid by corporations, domestic and foreign, out of income derived from property located and business transacted in the State of Wisconsin. The law specifically provides that such tax shall be deducted and withheld from such dividends payable to resident and nonresident stockholders by the payor corporation. The corporation declaring the dividend is also made liable for the tax, but is required to deduct it from the dividends payable to the stockholders.

The basic facts in connection with the assessments are not in dispute. The appellant is a Delaware corporation with its principal office and place of business in St. Paul, Minnesota. Its only operations in Wisconsin is in connection with a factory at Wausau, Wisconsin, where it manufactures roofing granules. It commenced actual operations in Wisconsin in 1930 and was duly qualified as a foreign corporation. Sales are made of the products from the Wisconsin operations through a sales office in Chicago, Illinois. All of these orders are confirmed at the St. Paul office and shipping instructions forwarded from the St. Paul office (R. 77). When products so manufactured are sold, the remittances are made directly to the home office at St. Paul and funds from such sales are deposited in the bank account of the appellant. Payrolls are prepared in St. Paul and are drawn on a Wausau, Wisconsin bank and a deposit equaling the amount of the payroll is forwarded to the Wausau, Wisconsin bank from St. Paul to cover the checks approximately at the time the checks representing the payroll

are forwarded (R. 77). The appellant, as a foreign corporation, reports such income as is taxable to the state of Wisconsin for income tax purposes on a calendar year basis (R. 38). All dividends upon which the attempt to tax involved in this controversy were levied were declared by the board of directors of the company at meetings held at St. Paul, Minnesota. The transfer agent for shares of stock is the First Trust Company of St. Paul, Minnesota (R. 22, 23, 77). Dividends paid by the appellant during the whole period involved in controversy on this appeal were paid to the transfer agent in St. Paul by check drawn on the St. Paul bank, and distributed by such bank through the mails to company stockholders by the transfer agent; no directors' meetings have ever been held in the state of Wisconsin (R. 22, 77). Only a small percentage of the outstanding stock of the appellant is owned by Wisconsin residents (R. 23, 47). The record shows that dividends are not paid out of the earnings of the company for the year immediately preceding the payment of the dividend, but are rather paid out of the general funds of the corporation. The dividends in question were paid pursuant to Section 34 of the Delaware Corporation Law, which provides as follows:

"The directors of every corporation created under this Chapter, subject to any restrictions contained in its Certificate of Incorporation, shall have power to declare and pay dividends upon the shares of its capital stock either (a) out of its net assets in excess of its capital as computed in accordance with the provisions of Section 14, 26, 27 and 28 of this Chapter, or (b) in case there shall be no such excess, out of its net profits for the fiscal year then current and/or the preceding fiscal year." (R. 79)

The dividends in question were pursuant to resolution of the board of directors declared and paid out of the surplus of the company (R. 39, 79).

Many stockholders in the company have only a small number of shares of stock and on the basis of the assessments as made a tax cannot be computed and withheld from the small stockholders in the exact amount thereof because the amount of tax would be a fractional amount of a cent (R. 30, 31). In making the assessments in question the Wisconsin Department of Taxation attempted to analyze the total surplus of the corporation on December 31st of the year preceding the year in which a particular dividend was paid, to ascertain how much Wisconsin income was in the surplus. In such alleged analysis, the Department analyzed surplus back to the date on which the corporation first commenced doing business in Wisconsin attempting to determine the total surplus at that time and then attempting to analyze from year to year the ratable contributions of earnings in Wisconsin to the surplus as of December 31st prior to the declaration of the dividend. It then determined the percentage of Wisconsin earnings in surplus to aggregate surplus and applied a fraction resulting from this ratio to total dividends paid by the corporation and taxed that portion of the dividend so allocated to Wisconsin (R. 8, 64-65, 68-69, 72A-73). The stock records of the company are maintained in Minnesota and Delaware and not in Wisconsin. The surplus of the company at the end of various years was invested in accounts, inventory, fixed assets, such as lands, buildings, machinery and equipment located in various states, and in cash (R. 32).

The Wisconsin Department of Taxation purporting to act under the Wisconsin privilege dividend tax law levied three separate additional assessments against the appellant as follows:

Dividends paid in the calendar year of 1936	\$2,220.60
Dividends paid in the calendar year of 1937	3,037.75
Dividends paid in the calendar years of 1938, 1939 and 1940	9,307.08
(R. 64, 68, 72A)	

Appropriate claims for abatement were filed with the Department of Taxation and denied. Thereafter, as provided by the laws of Wisconsin, the appellant petitioned the Wisconsin Board of Tax Appeals for review of assessments and reversal thereof. The matters were consolidated for hearing and a single record made up before the Board of Tax Appeals which affirmed the assessments so made, with modification of certain assessments, not material to the controversy in its present stage.

The appellant then appealed said determination of the Board of Tax Appeals to the Circuit Court for Dane County, Wisconsin (R. 83-97), and that court affirmed the decision and order of the Board of Tax Appeals (R. 99-100).

The appellant appealed from this decision and judgment of the Circuit Court for Dane County to the Supreme Court for the State of Wisconsin, the court of last resort in Wisconsin, and it affirmed the judgment so delivered. On the issue of whether a portion of the law was unconstitutional under the Fourteenth Amendment to the Constitution of the United States as being vulnerably retroactive and as such taking the property of the appellant and its stockholders without due process of law, the Supreme Court of the State of Wisconsin was evenly divided—three justices being of the opinion that the law was unconstitutional to the extent that it imposed a vulnerably retroactive tax, the other three justices being of the opinion that the law was constitutional in this respect.

Throughout all of these proceedings, the appellant has challenged the validity of the law as applied to dividends paid by it and particularly has it challenged the law and the tax assessments thereunder as applied to dividends paid by it on the ground that it takes its property and the property of the stockholders of the appellant without due process of law and in contravention to the Fourteenth Amendment of the United States because it imposes a tax beyond the taxing jurisdiction of the state of Wisconsin.

Appellant throughout the proceedings has further challenged the validity of the law as applied to it and its stockholders so far as it purports to reach the alleged Wisconsin income purportedly included in the payment of the dividend *regardless of when earned*, it being contended that in any event to the extent that the law and the purported tax attempts to reach so-called Wisconsin income in surplus for many years prior to the enactment of the law in 1935, that such law and tax takes the property of the appellant and its stockholders without due process of law and in contravention to the Fourteenth Amendment of the United States.

The Wisconsin Supreme Court in its decision in the instant case specifically ruled upon the constitutional questions so raised by the appellant, but denied it the relief prayed for although as hereinbefore pointed out on the constitutional retroactivity phase of the matter, the Wisconsin Supreme Court was evenly divided.

It is from this decision and judgment of the Wisconsin Supreme Court that the appellant has appealed.

#### IV.

#### Specifications of Error.

1. The Supreme Court of Wisconsin erred in failing to hold that Section 3, Chapter 505, Wisconsin Session Laws, 1935, as amended by Chapter 552, Wisconsin Session Laws, 1935, and as extended in operation by Chapter 309, Wisconsin Session Laws, 1937, and Chapter 198 of Wisconsin Session Laws, 1939, as applied to Minnesota Mining & Manufacturing Company and its stockholders under the existing facts was invalid as in conflict with the Fourteenth Amendment to the Constitution of the United States of America as imposing a tax beyond the taxing jurisdiction of the State of Wisconsin.

2. The Supreme Court of Wisconsin erred in failing to hold that the assessment of taxes involved in this proceeding pursuant to the provisions of Section 3, Chapter 505, Wisconsin Session Laws, 1935, as amended by Chapter 552, Wisconsin Session Laws, 1935 and as extended in operation by Chapter 309, Wisconsin Session Laws, 1937, and Chapter 198 of Wisconsin Session Laws, 1939, against the Minnesota Mining & Manufacturing Company, a Delaware corporation, under the existing facts, constituted a deprivation of property of Minnesota Mining & Manufacturing Company and its stockholders without due process of law and beyond the taxing power of the State of Wisconsin and therefore invalid as violative to the Fourteenth Amendment to the Constitution of the United States of America.

3. The Supreme Court of Wisconsin erred in failing to hold (split decision of State Supreme Court three to three which by rule of Wisconsin Supreme Court affirmed the trial court's decision) that Section 3, Chapter 505, Wisconsin Session Laws, 1935, (as amended by Chapter 552, Wisconsin Session Laws, 1935), and as extended in operation by Chapter 309, Wisconsin Session Laws, 1937, and Chapter 198 of Wisconsin Session Laws, 1939, so far as it purports to reach Wisconsin earnings of Minnesota Mining & Manufacturing Company without reference to the year in which they were earned, and for many years prior to the enactment of the law and from the time the corporation first operated in Wisconsin, are invalid as depriving the Minnesota Mining & Manufacturing Company and its stockholders of property without due process of law and therefore to this extent invalid as violative of the Fourteenth Amendment to the Constitution of the United States.

## ARGUMENT.

### Summary of Argument.

**POINT 1:** The Wisconsin privilege dividend tax law has now been definitely and finally construed by the Wisconsin Supreme Court as a privilege tax upon the stockholder, and not as an income tax upon the corporation. (*J. C. Penney Company vs. Tax Commission* (on remand), 238 Wis. 69, 73; *Blued vs. Wisconsin Foundry and Machine Co.*, 243 Wis. 221, 10 N. W. (2d) 142; *Wisconsin Gas and Electric Company vs. Department of Taxation*, 243 Wis. 216, 10 N. W. (2d) 140.) The majority decision of this Court in *State of Wisconsin vs. J. C. Penney Company*, 311 U. S. 435, 61 Sup. Ct. 246, 85 L. Ed. 267, which sustained the constitutionality of the law, was rendered before the Wisconsin Court had determined that the incidence of the tax was on the stockholder, it having at that time merely characterized the tax as a privilege tax. The majority opinion of this Court in the *Penney* case sustaining the law as constitutional only as a supplementary income tax on the corporation is not authority to support the constitutionality of the law as a privilege tax against a stockholder. Accordingly the whole foundation and basis on which constitutional justification for the law and tax was predicated in the *Penney* case has now been removed. The determination of the State Court that the incidence of the tax is on the stockholder and not on the corporation is binding on this Court. (*Federal Land Bank vs. Bismarck Lumber Co.*, 314 U. S. 95, 99, 62 Sup. Ct. 1; *Alabama vs. King and Booser*, 314 U. S. 1, 9, 10, 62 Sup. Ct. 43; *Colorado Bank vs. Bedford*, 310 U. S. 41, 52, 60 Sup. Ct. 800.) The mere fact that the construction now given to the law by the Wisconsin Supreme Court is contrary to that made in the majority decision in this Court in the *Penney* case before the Wisconsin

Court had decided upon whom the incidence of the tax rested, is immaterial, inasmuch as at that time the law not having been fully construed by the State Court, this Court had some latitude in construing the law. (*Meredith vs. Winter Haven*, 320 U. S. 228.) The law now having been finally and unequivocally construed by the Supreme Court of Wisconsin, this Court is bound to accept the law with the construction so given it by the Supreme Court of Wisconsin as a privilege tax upon the stockholder. (*Green vs. Neal's Lessee*, 6 Peters 291.) The construction now finally given the law by the Wisconsin Supreme Court is substantively different than the construction given the law by this Court in the *Penney* case and is not merely a difference in form. Furthermore, this Court under all the circumstances of this case is bound and required to accept the law as drawn by the Legislature and as construed by the Wisconsin Court and is not at liberty to reshape it to a form where it might constitutionally accomplish the same result. (*Oklahoma vs. Wells Fargo & Co.*, 222 U. S. 298, 302; *Home Savings Bank vs. Des Moines*, 205 U. S. 503, 519; *Chanler vs. Kelsey*, 205 U. S. 466, 482.) Accordingly the law must be accepted as a privilege tax upon the stockholder.

**POINT 2:** As a privilege tax on a foreign stockholder of a foreign corporation declaring and paying dividends outside the State of Wisconsin, the law as applied to appellant and its stockholders is clearly unconstitutional under the Fourteenth Amendment of the United States as taking property without due process of law.

If Wisconsin may not constitutionally directly impose its income tax upon income payable to nonresident stockholders of a foreign corporation, it is *a fortiori* clearly unconstitutional for it to impose a tax upon such stockholders at the time of a payment of a dividend to the stockholders which the corporation is required to deduct.

The privilege of earning income in the State of Wisconsin by the corporation is entirely separate and distinct from the privilege of receiving a dividend out of income in the surplus account. The privilege of earning the income of the corporation in Wisconsin is a privilege granted to the corporation that can be taxed and has been taxed against the corporation under the general income tax laws. The privilege of declaring and paying the dividend and the privilege of devolving the income earned in Wisconsin in prior years to stockholders of a foreign corporation is a privilege neither conferred nor controlled by Wisconsin and may not be taxed by it. (*Provident Savings Life Assurance Society vs. Kentucky*, 239 U. S. 103, 111, 113; *Connecticut General Life Insurance Co. vs. Johnson*, 303 U. S. 77, 58 Sup. Ct. 436.)

The law and tax cannot be sustained against the stockholders of a foreign corporation merely because the foreign corporation has enjoyed certain privileges in Wisconsin (which privileges have already been taxed), without unwarranted and complete disregard of the corporate entity which has been legitimately exercised. There is no principle of justice which requires the disregard of the corporate entity in order to sustain the dividend tax. (*New Colonial Ice Co. vs. Helvering*, 292 U. S. 435.) The general income tax under the laws of Wisconsin has been imposed upon the corporation based upon the conception of the appellant as a separate entity, and after such imposition the State of Wisconsin should not be allowed to disregard the corporate entity for the purpose of sustaining the privilege dividend tax against the stockholder.

**POINT 3:** In the event it is determined that Wisconsin had jurisdiction to levy any tax on the foreign stockholder of a foreign corporation on the ground that Wisconsin gave protection to the corporation in earning the income used in such dividend—then so much of the law as attempts to tax

the earnings in surplus which had accumulated prior to the enactment of the law is unconstitutional under the Fourteenth Amendment as being vulnerably retroactive. The only jurisdictional basis ever urged to support the law and tax is because of the protection which Wisconsin gave to the earning of the income. Such protection can, in the nature of things, be given only in the year in which the income is earned. Under the formula used by the Wisconsin Department of Taxation in levying the tax, all so-called "income" from Wisconsin in surplus *regardless of when earned* is subject to the tax. To "charge" by way of tax, for the privilege Wisconsin gave to the corporation in the earning of income years before the enactment of the tax law, results in a tax so vulnerably retroactive as to result in the taking of the property of the appellant and its stockholders without due process of law.

### **Preface Reflecting Present Status of the Constitutional Aspects of Wisconsin Privilege Dividend Tax.**

An orderly presentation of the issues involved on this appeal requires as a background a summarization of certain proceedings heretofore had in this Court and in the Wisconsin Supreme Court which involved certain phases of the Wisconsin privilege dividend tax law.

Certain phases of the Wisconsin privilege dividend tax law have heretofore been before this Court in the cases of *State of Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435, 61 Sup. Ct. 246; *State of Wisconsin vs. Minnesota Mining & Manufacturing Co.*, 311 U. S. 452, 61 Sup. Ct. 253; and *State of Wisconsin vs. F. W. Woolworth Co.*, 311 U. S. 422, 61 Sup. Ct. 395.

Those cases involved a review of a determination of the Supreme Court of the State of Wisconsin which found the Wisconsin privilege dividend tax law as applied to foreign

corporations unconstitutional under the Fourteenth Amendment of the Constitution of the United States. This Court by a five (5) to four (4) decision—Chief Justice Hughes, Mr. Justice McReynolds, Mr. Justice Roberts and Mr. Justice Reed, dissenting—reversed the Wisconsin Supreme Court, the majority of the Court speaking through Mr. Justice Frankfurter, holding that the practical operation of the law and tax was to impose an additional income tax on corporate income when paid out, and holding that the fact that the Wisconsin Supreme Court had “labeled” the law a tax on the privilege of declaring dividends rather than as a supplementary income tax on the corporation did not vitiate the tax, and that Wisconsin had the power to levy such a supplementary income tax on the corporation because it had given protection to the earning of the income (*State of Wisconsin vs. J. C. Penney Co.*; 311 U. S. 435 at 444.) The dissenting division of the Court, however, challenged the construction of the law given in the majority opinion and insisted that the tax was strictly an excise tax and that the tax was a tax against stockholders and as such was clearly invalid under the Fourteenth Amendment to the Constitution of the United States as to a foreign corporation. We submit that it is apparent from a reading of the decision, that the majority opinion assumed that if the tax was a tax against the stockholder it could not be sustained. It seems further apparent that the controversy between the majority and minority divisions of this Court was based primarily upon a difference of opinion as to a proper construction of the law rather than upon the application of constitutional concepts.

The taxes involved in the litigation heretofore before this Court had been assessed against the corporations, by the application of a statutory presumption that dividends of a foreign corporation were presumed to have been paid

out of earnings of the company attributable to Wisconsin under the general income tax statute for the year immediately preceding the declaration of the dividend in the absence of proof to the contrary. (See Sub-Section 4 of Section 3, Chapter 505, Laws of 1935.) This Court in the *J. C. Penney Company* case, *Minnesota Mining and Manufacturing Company* case, and *F. W. Woolworth Company* case remanded the cases to the Supreme Court of Wisconsin for the determination of such questions as were open in light of the opinion so rendered by this Court (*State of Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435, 446).

The Wisconsin Supreme Court on remand (*J. C. Penney Co. vs. Tax Commission* and companion cases, 238 Wis. 69) held and determined that the statutory presumption on which the taxes were assessed in those cases had been erroneously applied because all of the litigants had paid the dividends out of surplus and this circumstance rebutted the statutory presumption that the dividends were paid out of the prior year's earnings. The Wisconsin Supreme Court accordingly remanded the litigation to the Tax Commissioner for further computation of the tax.

On remand the Wisconsin Supreme Court vehemently denied that the tax was an income tax on the corporation as indicated by the majority decision of this Court in the *Penney* case and postulated that if it was an income tax, it was an income tax on the stockholder and as to a non-resident stockholder, void under the Wisconsin constitution.

The tax against the Minnesota Mining & Manufacturing Company involved in the prior litigation involved only a tax on the dividends paid by that company in the calendar year of 1936, and the tax for that year has now been computed on an entirely different basis (so-called surplus analysis basis, instead of statutory presumption basis as originally).

Because on remand, the Wisconsin Supreme Court reversed its decision with directions to remand each case to the Tax Commissioner because of incorrect computation, the taxpayer litigants there involved, inasmuch as such determination was not *final*, had no right or opportunity to appeal from the decision of the Court on remand to this Court to urge that Mr. Justice Frankfurter's construction of the law was erroneous, or at least that the Wisconsin Court had subsequently construed the law to place the incidence of the tax on the stockholder, otherwise than as construed by this Court in the *Penney* case, and inasmuch as the decision on the Federal constitutional question was predicated solely on a construction of the law as a supplementary corporate income tax, that a different result should be reached. It should here be said however in justification of Mr. Justice Frankfurter's approach to the matter, that at the time of the decision of this Court in the *J. C. Penney* case the Wisconsin Court had not determined the incidence of the tax. It had to a certain extent characterized the tax as a transaction tax, but it had not at that time, as it has today, unqualifiedly construed the incidence of the tax to be upon the stockholder as distinct from the corporation.

It is unqualifiedly clear, however, that on the decision on remand and in a series of subsequent cases, the Supreme Court of Wisconsin by its construction of the law has removed the basis on which this Court upheld the law and tax in the *Penney* case, by denying a construction to the law which made it an income tax against the corporation.

In short, a basic conflict in the construction of the law existed between that given it by the majority of this Court speaking through Mr. Justice Frankfurter, and that given it in the dissenting opinion of this Court and by the Wisconsin Supreme Court on remand and in later cases.

Judge Alvin C. Reis of the Circuit Court for Dane County, in his decision in the companion case of *International Harvester Company vs. Wisconsin Department of Taxation*, No. 620, October 1943 term, has succinctly, forcefully, and accurately analyzed this basic conflict as follows:

"We agree with counsel for the International Harvester Company that an immaculate dilemma has been created.

In the first Penney case the Supreme Court held the tax to be a transaction tax or tax on 'privilege', as in terms it so states; and since the transaction happened and the privilege was exercised outside of Wisconsin, in the case of a foreign corporation such as this one, the Wisconsin court held the tax unconstitutional, being violative of due process.

When however this case reached the Supreme Court of the United States, the tribunal regarded this tax as a 'supplementary income tax' upon the corporation and hence clearly within the power of the state to impose and not infringing upon the fourteenth amendment.

In the third and final round of the battle thus far, i.e., remand from the United States Supreme Court to the Wisconsin court, our local court followed the United States Supreme Court upon the issue of constitutionality *because it had to do so*. That pithes a delicate point rather abruptly but no one will question the accuracy of our assertion.

The Supreme Court of Wisconsin however, in this last decision, refused to recede from its former position that this was an excise or privilege tax. It militantly maintained that it was its right, and its alone, to say what this tax was; and that such was not the province of the Supreme Court of the United States. And thereupon and in the face of the highest federal court declaration that the tax here involved was a 'supplementary income tax' upon the corporation, the Wisconsin court unequivocally declared: "*In no sense and to no extent whatever, is it a tax upon the income of the corporation.*" (Our italics.)  
(*J. C. Penney Company vs. Tax Commission*, 238 Wis. 69, 73.)

We can not settle this dispute. That rests far beyond our hands.

The Wisconsin court insists that the tax is a transaction tax, which under the Federal constitution makes it unconstitutional because based on out-of-state transactions. But the United States court majority opinion disregards it as a transaction tax and sets the tax up as an additional corporate income tax, the validity of which is obvious.

The Supreme Court of Wisconsin, as noted, however, will not accept it as an income tax on the corporation. Furthermore, it postulates that if it is an income tax on individuals, it is unconstitutional *under the state constitution*, because the individuals are beyond the jurisdiction of Wisconsin to tax.

"It is perfectly true that the tax cannot be sustained as an income tax under the law of this state."  
—Thus spoke our own Supreme Court.

*J. C. Penney Company vs. Tax Commission*, 238 Wis. 69, 72.)

Therefore, as an income levy, the tax is completely *persona non grata* in this state,—an unwanted black sheep in the Wisconsin court's backyard.

Here then is the deadlock: If the tax is a transaction tax, as Wisconsin's court says it is, then it is void under the *Federal* constitution; and the federal court should so hold it. If on the other hand it is an income tax, it can be an income tax only on individuals, according to the Wisconsin court, and then it becomes void under the state constitution; and the state court should so hold it." (R-50 et. seq.—Int. Harvester case.)

A comparison of the language in the majority opinion of this Court and of the dissenting opinion of this Court and of the language of the Wisconsin court on remand and in later cases illustrates clearly and graphically this basic conflict of construction, and also makes it readily apparent that the privilege dividend tax was upheld in this Court only as a supplementary corporate income tax:

*See Folded Insert — Opposite This Page.*



**Mr. Justice Frankfurter's Opinion, Penney Case (61 S. Ct. 248):**

"The practical operation of this legislation is to impose an additional tax on corporate earnings within Wisconsin but to postpone the liability for this tax until such earnings are paid out in dividends."

\* \* \*

(P. 249)

"\* \* \* by the privilege dividend tax of 1935 Wisconsin superimposed upon this income tax a tax upon corporate income that is paid out."

\* \* \*

"The case thus reduces itself to the inquiry whether Wisconsin has transgressed its taxing power because its supreme court has described the practical result of the exertion of that power by one legal formula rather than another—has labeled it a tax on the privilege of declaring dividend rather than a supplementary income tax."

**In Minn. Mining & Mfg. Co. Case (311 U. S. 452, 453):**

"But it is too late in the day to find offense to that Clause because a state tax is imposed on corporate net income

**Mr. Justice Robert's Dissent, Penney Case (61 S. Ct. 251):**

"It is said that the challenged exaction is merely an additional income tax—this notwithstanding that the tax is not called an income tax, has been held by the highest court of Wisconsin not to be an income tax but an excise tax upon a privilege. \* \* \*"

\* \* \*

(P. 252)

"By the very terms of the Act the tax is laid not on the corporation, but on the stockholders receiving the dividend, and, by confession, thousands of stockholders are not residents of Wisconsin."

\* \* \*

(P. 252)

"We are now told that this is not a fair exposition of the law, but that on the contrary and in the teeth of the known facts what Wisconsin did was to lay a supplementary income tax upon foreign corporations."

**Chief Justice Rosenberg's Opinion, Penney Case on remand (238 Wis. 69 at 73):**

"In no sense and to no extent whatever is it a tax upon the income of the corporation."

\* \* \*

(238 Wis. 69 at 73)

"There is no provision in the Wisconsin statute for taxing disbursements as income. The income of the corporation was taxed by the state when it was received. If the State sought to tax the corporate income at a higher rate, all that it was required to do was to increase the rate."

(238 Wis. 69 at 72)

"If there has been a shifting of labels in this case, it was not done by this court. It is perfectly true that the tax cannot be sustained as an income tax."

**Mr. Justice Wickhem, Wis. Gas. & Elec. Co. vs. Dept. of Taxation (243 Wis. 216, 220):**

"The real question in this case is: On whom is the actual burden of this tax laid? This question can have but one answer. The statute specifically puts it upon the stockholder."

\* \* \*

(243 Wis. 216, 224)

"We are certain \* \* \* (1) That the burden of the tax is specifically laid upon the stockholder."

**Mr. Justice Wickhem, Blied vs. Wis. Fndry. & Mach Co. (243 Wis. 221, 223):**

"The decision in Wis. Gas & Elec. Co. vs. Dept. of Taxation \* \* \* requires that the judgment in this case be affirmed since the specific requirements of the statute which we hold to be valid are that the tax be withheld and deducted from the dividend payable to a stockholder."



The present status of the litigation is also reflected in an article in 28 *Marquette Law Review*, page 23, "Wisconsin Privilege Dividend Tax" by William Smith Malloy.

In short the conclusion is inescapable that when the matter was before this Court in the *Penney* case the law was held to be a supplementary *income* tax on the *corporation*,—whereas it has now been unequivocally determined by the Wisconsin Supreme Court to be a *privilege* tax upon the *stockholder*.

**Point I:** The law as now authoritatively construed by the Wisconsin Supreme Court places the incidence of the tax on the stockholder and not on the corporation. Accordingly, the decision of this Court in the case of *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435, is not decisive of the present controversy.

As indicated in the preface to this brief, as a result of a series of recent decisions of the Wisconsin Supreme Court, the issues now confronting this Court on the constitutional problems of this case are essentially different from those presented at the time that the constitutionality of the Wisconsin privilege dividend tax law was originally considered in *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435.

(a) There can be no question but what the law as now construed by the Supreme Court of Wisconsin imposes a privilege tax upon the stockholder, and not upon the corporation.

We assert dogmatically that there is and can be no question but what the Wisconsin Supreme Court has now construed the law in question as a *privilege tax upon the stockholder*, and has specifically negatived the tax as an *income* tax or as a tax of any kind or nature against the cor-

poration. This construction given the tax law is not a matter of "labels", — it is one of basic substance. From it we find the operating incidence of the tax and as stated by Mr. Justice Frankfurter in the *J. C. Penney* case *supra*, at page 444:

" . . . For constitutional purposes, the decisive issue turns on the operating incidence of a challenged tax."

In the preface of this brief, we have attempted to point out in a more or less summary manner, the status of the litigation in this Court and in the Wisconsin Supreme Court, as it has affected a determination of the incidence of the tax created by the law under consideration.

At the time this Court had before it the case of *J. C. Penney Co. supra*, the Wisconsin court had not specifically determined the incidence of the tax to be upon the stockholder. It had, "characterized" the tax as a transaction tax. It appeared from the statute that the operating incidence of the tax was against the stockholder and not against the corporation, but at that time the Wisconsin court had had no occasion to specifically construe the law in this respect.

Since the decision by this Court in the *J. C. Penney Co.* case, *supra*, however the Wisconsin court has unequivocally determined the incidence of the tax to be upon the stockholder, and has specifically negated the incidence being upon the corporation.

In the opinion of the Wisconsin Supreme Court on remand in the case of *J. C. Penney Co. vs. Tax Commission*, 238 Wis. 69, it immediately became apparent that the Wisconsin court refused to accede to a construction of the statute as an income tax of any kind or nature, and further specifically refused to accede to a construction that the law imposed a tax upon the corporation. In the course of the

opinion in that case by Chief Justice Rosenberry he said, among other things, at pages 72 and 73:

" \* \* \* *If there has been a shifting of labels in this case, it was not done by this court. It is perfectly true that the tax cannot be sustained as an income tax under the law of this state.* Under our constitutional amendment authorizing the levying of an income tax, sec. 1, art. VIII, Const., it has been consistently held that an income tax is a burden laid upon the recipient of an income and the amount of the tax is measured by the amount of the income. *State ex rel. Sallie F. Moon Co. vs. Wis. Tax Comm.* (1917), 166 Wis. 287, 163 N. W. 639, 165 N. W. 470. Under its laws this state cannot and it does not undertake to tax the income of citizens of other states who are not doing business in this state. Under the terms of the statute under consideration no tax is levied until a dividend is declared. When the dividend is declared the dividend belongs to the stockholder. It is a debt of the corporation for the recovery of which the stockholder may maintain an action. Inasmuch as the tax cannot be levied until the dividend is declared if it is not a tax on the privilege of declaring and receiving a dividend as we hold it to be, then it must be a tax on the recipient, a person not engaged in doing business in this state nor a resident thereof. *In no sense and to no extent whatever, is it a tax upon the income of the corporation.*" (Italics ours)

He further said at page 73:

" \* \* \* There is no provision in the Wisconsin statutes for taxing disbursements as income. The income of the corporation was taxed by the state when it was received. If the state sought to tax the corporate income at higher rate, all that it was required to do was to increase the rate."

While the decision of the Wisconsin Supreme Court on remand quite conclusively negated the tax law as an income tax or a tax of any kind or nature against the corporation, a subsequent series of cases even more clearly

and conclusively eliminates any doubt whatsoever about the matter and specifically hold that the incidence of the tax created by the law is upon the stockholder and not the corporation.

In the case of *Wisconsin Gas & Electric Co. vs. Department of Taxation*, 243 Wis. 216, 10 N. W. (2d) 140,—it was contended that a corporation could claim a deduction from gross income for Wisconsin income tax purposes of amounts paid for Wisconsin privilege dividend taxes, among other reasons because this Court in the *Penney* case had decided the tax to be upon the corporation. The Wisconsin Supreme Court however denied the corporation the right to deduct the tax, holding that it was a tax not on the corporation, but upon the stockholder, and in the course of the Wisconsin court's opinion Mr. Justice Wickhem stated at page 219 et seq. as follows:

“ \* \* \* The real question in this case is: On whom is the actual burden of this tax laid? This question can have but one answer. The statute specifically puts it upon the stockholder. The corporation is directed to deduct the tax from the dividends, and if it does as it is required to do, it sustains no expense and consequently may not, in any event, deduct the tax from its gross income.”

Further, at page 220 the Court said:

“ \* \* \* We are certain of three things: (1) That the burden of the tax is specifically laid upon the stockholder; (2) that the corporation declaring the dividend must deduct the tax from the dividend and may not under any circumstances treat the tax as a necessary expense of doing business; (3) that the power to levy the tax so construed was authoritatively established in the *Penney* case, *supra*.” (Italics ours)

And, even more specifically did the Wisconsin Supreme Court hold the tax to be solely upon the stockholder and not on the corporation in the case of *Blued vs. Wisconsin Foun-*

*dry and Machine Co.*, 243 Wis. 221, 10 N. W. (2d) 142. In that case a preferred stockholder brought suit against the corporation to recover a deduction that the corporation had made from the preferred stockholder's dividend for the purpose of paying the Wisconsin privilege dividend tax. The contention was made by the stockholder that this Court in the *Penney* case had construed the tax as one on the corporate earnings and the corporation alone was made liable for the tax and penalties and interest for failing to pay it, and that there was no personal liability created in the tax act upon the stockholder, and that accordingly the tax was upon the corporation and not upon the stockholder. The Wisconsin Supreme Court however on the authority of the *Wisconsin Gas and Electric Company* case, *supra*, denied recovery to the preferred stockholder of the tax so deducted:

" \* \* \* since the specific requirements of the statute which we hold to be valid are that the tax be withheld and deducted from the dividend payable to a stockholder." (243 Wis. 221, 223)

As indicated the construction given to the law by the Wisconsin Supreme Court is basically and substantively different from that given the law by this Court in the *Penney* case. This difference is not one of form or of 'characterization'. A deliberate determination of the incidence of the tax has been made by the Wisconsin Supreme Court as being upon the stockholder.

- b) **This Court under the circumstances of this case is clearly bound by the construction given the law by the Supreme Court of Wisconsin.**

It is of course a fundamental principle of law that a state court is the final authority in the matter of construction of state laws. This is equally true where the issue is as

to the incidence of a particular tax imposed by state law. This recognized basic principle of law has been reiterated by members of the present Court only recently on several occasions.

Mr. Chief Justice Stone in considering the incidence of a sales tax for constitutional purposes in the case of *State of Alabama vs. King and Boozer*, 314 U. S. 1, at pages 9 and 10 said:

“ \* \* \* Who, in any particular transaction like the present is a ‘purchaser’ within the meaning of the statute, is a question of state law on which only the Supreme Court of Alabama can speak with final authority.”

And Mr. Justice Murphy in considering the incidence of a sales tax for constitutional purposes in the case of *Federal Land Bank vs. Bismarck Lumber Co.*, 314 U. S. 95, at page 99 said:

“The Supreme Court of North Dakota has held that the sales tax is laid on the purchaser. *Jewel Tea Co. vs. State Tax Commissioner*, 70 N. D. 229, 293 N. W. 386. This holding was reaffirmed in the decision below. These determinations of the incidence of the tax by the state court are controlling, and respondents concede the point.”

And, Mr. Justice Reed in the case of *Colorado National Bank vs. Bedford*, 310 U. S. 41, which involved the matter of incidence of a particular state tax said at page 52:

“The person liable for the tax, primarily, cannot always be said to be the real taxpayer. The taxpayer is the person ultimately liable for the tax itself. The funds which were received by the state came from the assets of the user, and not from the federal instrumentality, the bank. The Colorado Supreme Court holds the user as the taxpayer. The determination of the state court as to the incidence of the tax has great weight with us and, when it follows logically the language of the act, as here, is controlling.”

Citations in support of the above principle of law could be multiplied almost indefinitely, a few of the leading cases being as follows:

*The Commercial Bank of Cincinnati vs. Buckingham's Executors*, 5 How. 317, 343, 12 L. Ed. 169 (1847);

*Hotel and R. E. Int. A. vs. Wis. E. R. Bd.*, 315 U. S. 437, 440-441 (1942);

*Brinkerhoff-Faris Trust and Sav. Co. vs. Hill*, 281 U. S. 673, 74 L. Ed. 1107 (1930);

*Phoenix Ins. Co. vs. Gardiner*, 78 U. S. 204, 206, 20 L. Ed. 112;

*Montreal ex rel Pearson vs. Probate Court*, 309 U. S. 270, 273, 84 L. Ed. 744;

*Rawlins vs. Georgia*, 201 U. S. 638, 639, 50 L. Ed. 899.

There is a qualification to the rule herein cited not applicable to the present state of the controversy.\*

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\* Although not expressly called such, there appears to be a well established qualification to the rule above noted; to the effect that the United States Supreme Court has the power to disregard the characterization placed upon a statute by a state court of last resort, when it finds that the true meaning of a statute is such as to **encroach upon the federal constitution**: *Federal Land Bank vs. Crosland*, 261 U. S. 374; *Carpenter vs. Shaw*, 280 U. S. 363; *St. Louis Compress Co. vs. Arkansas*; 260 U. S. 346; *Macallen Co. vs. Massachusetts*, 279 U. S. 620; *Hanover Fire Ins. Co. vs. Carr*, 272 U. S. 494, 509. It seems quite apparent that this limited power given to this Court to construe a statute (except in instances where the statute has not already been construed by the state court), arises **only** from the duty of this Court to **prevent encroachment** by the States upon the federal constitution. It is an incident, and can only be exercised as an incident, of the power to prevent encroachment on the federal constitution. (*Truax vs. Corrigan*, 257 U. S. 312, 324).

Another accepted rule in testing the constitutionality of a statute is that this Court is required to accept a tax law as drawn by the legislative body enacting it and is not at liberty to sustain a law by reshaping it to a form where it might constitutionally accomplish substantially the same result.

This rule was succinctly stated and recognized by Mr. Justice Holmes in *Oklahoma vs. Wells Fargo and Co.*, 222 U. S. 298 at 302 where the learned justice said:

“Neither the court below, nor this court can reshape the statute simply because it embraces elements it might have reached if it had been drawn with a different measure and intent.”

And this Court in *Home Savings Bank vs. Des Moines*, 205 U. S. 503 at 519 said:

“If the State has not the power to levy this tax, we will not inquire whether another tax which it might lawfully impose would have the same ultimate incidence. Precisely the same argument was made and rejected in *Owensboro National Bank vs. Owensboro*, 173 U. S. 164.”

And the rule is further recognized by Mr. Justice Holmes, with whom Mr. Justice Moody concurred in a dis-

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Historically, the function of this Court has been to defend the rights of the people guaranteed by the federal constitution from encroachment by the states. Indeed, not until December 23, 1914, (38 Stat. 790) was a review from a decision of a state court upholding a constitutional right even allowed. (See Frankfurter, 39 Harvard Law Review 1046, 1049-1057). Even now such review is allowed only by certiorari, whereas an appeal lies of right where the constitutional guarantee has not been sustained. In any event this so-called qualification to the general rule that this Court is bound by the construction given a law by the state court is not applicable in the instant case since the state court has now clearly “construed” the law and has not merely characterized the law.

nting opinion in *Chanler vs. Kelsey*, 205 U. S. 466 at page 2, where it is said:

“And I also repeat that it has no bearing upon the matter that by a different law the state might have derived an equal revenue from these donees in the form of a tax.”

The above rules must be respected in the instant case. This Court being bound by the construction of the law as given it by the state court neither has the right to consider its constitutionality as a supplementary corporate income tax nor indeed as any other tax against the corporation, but solely as a privilege tax against the stockholders.

Because the legislature might have enacted a law which could be constitutionally valid (i.e. a supplementary corporate income tax) does not justify this court in sustaining the instant law on the ground that it might have been enacted in a different form under which it would have produced the same amount of revenue.

Even were this Court free to construe the law and the incidence of the tax as an original proposition, we submit that notwithstanding the construction which the majority decision gave the law in the *Penney* case,— the law itself clearly places the incidence of the tax on the stockholder, and were the matter open for the determination of this court, that so much of the decision in the *Penney* case as construed the law as a tax against the corporation should be reconsidered and corrected. As Mr. Justice Frankfurter said in *Helvering vs. Hallock*, 309 U. S. 106 at page 121:

“This Court, unlike the House of Lords, has from the beginning rejected a doctrine of disability at self-correction.”

- (c) This Court in the case of *Wisconsin vs. J. C. Penney Co.*, 311 U. S. 435, sustained the law only as imposing a supplementary income tax on the corporation,—not as a privilege tax on the stockholder. The law now having been authoritatively construed by the Wisconsin Supreme Court as a privilege tax on the stockholder, the Wisconsin court was in error in assuming that the decision of this Court in the Penney Case determined the issues of constitutionality.

As indicated in an earlier portion of this brief, at the time that this law was before this Court in *Wisconsin vs. J. C. Penney Co.*, *supra*, the Wisconsin Court had not had occasion to decide upon whom the privilege dividend tax was imposed, having merely held there could be no constructive situs in the State of Wisconsin for an excise tax on the transaction of declaring and receiving dividends. In short, the Wisconsin Supreme Court at that time had not finally construed the Wisconsin privilege dividend tax and determined the incidence of the tax levied thereunder. It had merely characterized the tax as a privilege tax. This Court held that it was not bound by the characterization of the statute so far as that characterization might bear upon the question of its constitutional validity. Since the State Court had not finally determined whether the tax was upon the corporation or the stockholder, this Court had some liberty to construe the statute until the determination of the matter by the State Court.

*Erie R. R. Co. vs. Tompkins*, 304 U. S. 64, does not relieve Federal Courts of the responsibility of construing State laws in all cases within their jurisdiction when there has not been a construction by the State Court. This principle was recognized in the recent case of *Meredith vs. Winter Haven*, 320 U. S. 228, in which the Circuit Court had dismissed an appeal in a diversity case because State law concerning the

ability of a Florida municipality on its refunding bonds was not clear. At page 237 this Court recognized the aforementioned responsibility in the following language:

"Accepting this responsibility, as was its duty, this Court has not hesitated to decide questions of state law when necessary for the disposition of a case brought to it for decision, although the highest court of the state had not answered them, the answers were difficult, and the character of the answers which the highest state courts might ultimately give remained uncertain. (citations omitted)"

It is to be noted that the Wisconsin statute lays a tax on "the privilege of declaring and receiving dividends"; and this concept involves not only two separate and distinct acts, but also the acts of different parties. Confronted with a somewhat ambiguous statute which had not been construed by the State Court, at least as to the incidence of the tax, it was the duty of this Court to construe the statute if possible so that the law might be held constitutional. The Supreme Court does not presume that a State Court will so construe its statute as to render it unconstitutional. As this Court said in *Utah Power & Light Co. vs. Pfof*, 286 U. S. 165, at 186:

"Primarily, the construction of these provisions of the statute is for the State Supreme Court, and we cannot assume in advance that such a construction will be adopted, or such an application made of these provisions, as to render them obnoxious to the federal constitution."

See also:

*Mountain Timber Company vs. Washington*, 243 U. S. 219, 246;

*Allen Bradley Local vs. Board*, 315 U. S. 740, 746;

*Plymouth Coal Company vs. Pennsylvania*, 232 U. S. 531, 546;

*Bachtel vs. Wilson*, 204 U. S. 36, 40.

In accordance with these well established principles, Mr. Justice Frankfurter stated in the *Penney* case at page 443 of 311 U. S. that "• • • the descriptive pigeonhole into which a state court puts a tax is of no moment in determining the constitutional significance of the exaction". In its effort to uphold the Wisconsin statute this Court construed the privilege dividend tax as a "supplementary corporate income tax", and as such held it to be constitutional.\*

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\* The Court's information as to the Wisconsin income tax system was apparently primarily derived from the case of *Welch vs. Henry*, 305 U. S. 134, which upheld a Wisconsin tax imposed in 1935 on certain 1933 dividend which had been exempt when received. The Court stated that the tax gained "nourishing significance" from the exemption of these dividends but it did not note that the Wisconsin statute permitted the deduction from gross income only of dividends from corporations whose principal business was attributable to Wisconsin, which was defined as meaning corporations which derived 50% or more of their entire net income or loss from Wisconsin (Section 71.04 (4), Revised Statutes of Wisconsin, 1933). Since only a small portion of J. C. Penney's income was attributable to Wisconsin, the opinion of this Court in this particular case was based upon an apparent misconception of the Wisconsin Income Tax Law. It is obvious that the privilege dividend tax was designed partially in order to retain a favorite treatment of the stockholders of domestic corporations (which received more than 50% of their income from within the state), and yet at the same time to obtain a single small income tax on dividends accruing to such stockholders. The income accruing to stockholders of most foreign corporations residing in Wisconsin bears three income taxes (corporate income, privilege dividend, and personal income), while that of most domestic corporations bears only two taxes (corporate income and privilege dividend). The privilege dividend tax law has the effect of imposing a double personal income tax upon resident stockholders of foreign corporations, yet, because of the deduction of one of the taxes at the source, the stockholder does not realize quite as clearly as it otherwise might that he is

It is submitted that neither the majority opinion by Mr. Justice Frankfurter nor the dissenting opinion by Mr. Justice Roberts regarded the decision of the Wisconsin Supreme Court as a construction of the Privilege Dividend Tax Act, at least as far as the incidence of the tax was concerned. Mr. Justice Roberts agreed that this Court "• • • disregards mere names and descriptive epithets" (311 U. S. at page 447), but held that only by ignoring the express terms of the statute could the tax be regarded as a supplementary corporate income tax. He reasoned that if it could be considered an income tax in any sense, it was upon stockholders, and obviously bad.

As heretofore indicated the Wisconsin Supreme Court on remand in the *Penney* case and in a series of subsequent cases refused to accede to the construction given the law by this Court, and construed the law as a privilege tax on the stockholder.

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paying two taxes. If the States in which non-resident stockholders reside impose an income tax, this income likewise bears three taxes. From the foregoing it is plain that when the question of obtaining further revenue came before the Wisconsin Legislature, and exempt dividends of domestic corporations were suggested as a likely source of additional revenue, a scheme was devised which satisfied the State because it secured the revenue required and likewise satisfied the holders of large blocks of stock in local enterprises because they avoided the payment of the progressive income tax and the surtax which otherwise would almost certainly have been required. In other words a compromise was entered into between politically potent Wisconsin interests at the expense of the stockholders of corporations such as the appellant, which conducts less than half of its business within the state. The privilege dividend tax was designed not to correct the unfairness in regard to surtaxes mentioned by this Court, but to expressly perpetuate it. We submit that this explanation should go far to destroy any particular significance which this Court may have discovered in considering the privilege dividend tax in connection with the Wisconsin income tax system.

The only ground upon which the privilege dividend tax act was ever sustained in this Court has thus been removed by the Wisconsin Supreme Court. This Court is now presented with a construction by the Wisconsin Court that the incidence of the privilege dividend tax is upon stockholders, and as Mr. Justice Frankfurter stated in the *J. C. Penney* case, *supra*, at page 441:

“ \* \* \* For constitutional purposes, the decisive issue turns on the operating incidence of a challenged tax  
\* \* \* ”

As indicated in an earlier section of this brief, the construction of the privilege dividend tax act by the Wisconsin Court is binding on this Court, and may not be rejected even though this Court does not agree with its reasoning. The construction now given the law by the Wisconsin Court as distinct from its earlier characterization of the law, is diametrically opposed to the construction given the law by this Court in the *Penney* case. Other courts, which have considered this Court's opinion in the *J. C. Penney* case, have considered that the tax was upheld *only* as a supplementary corporate income tax. (See *Wisconsin Gas and Electric Co. vs. Commissioner of Internal Revenue*, 46 F. Supp. 929 at 930. (Rev'd. 138 F. (2d) 597, and now before this Court on certiorari for decision); *Montreal Mining Company vs. Commissioner*, Docket No. 106876, 2 T. Ct., No. 85 (September 16, 1943)).

In *Fidelity Trust Co. vs. Field*, 311 U. S. 169, the Circuit Court of Appeals had held that it was not bound to follow the ruling of intermediate State Courts on the effect of certain New Jersey statutes. At page 178 this Court stated:

“ Here, the question was as to the construction and effect of a state statute. The federal court was not at liberty to undertake the determination of that question on its own reasoning independent of the con-

struction and effect which the State itself accorded to its statute."

This Court takes cognizance of any change in an interpretation of local statutes which occurs during the course of a litigation. (*Vandenbark vs. Owens-Illinois Glass Co.*, 311 U. S. 538, 542; cf. *Blair vs. United States*, 300 U. S. 55.) Since the Wisconsin Supreme Court has now finally determined the incidence of the tax under the Privilege Dividend Tax Law, the original decision of this Court must be reconsidered in the light of that determination. This is the principle established by the old case of *Green vs. Neal's Lessee*, 6 Peters, 291, in which the Court said at page 299:

"If the construction of the highest judicial tribunal of a state form a part of its statute law, as much as an enactment by the legislature, how can this court make a distinction between them? There could be no hesitation in so modifying our decisions as to conform to any legislative alteration in a statute; and why should not the same rule apply where the judicial branch of the state government, in the exercise of its acknowledged functions, should, by construction, give a different effect to a statute from what had first been given to it."

See also *Fairfield County vs. County of Gallatin*, 100 U. S. 47, in which this Court reversed a prior opinion on a similar issue upon having a controlling State decision called to its attention.

The construction adopted by this Court in the *Penney* case had no effect whatever on the final meaning to be assigned by the State Court to the local statute (*Meredith vs. Winter Haven*, *supra*, at 237; *Union Pacific R. R. Co. vs. Weld County*, 247 U. S. 282, 287). The Wisconsin Supreme Court was not constrained from adopting another construction of the Act, and now that such interpretation has been adopted, this Court must inquire into the constitutionality of the act as now construed by the State Court.

Although the Wisconsin Supreme Court did not concur in the view of this Court as to jurisdiction, and indeed apparently did not consider that the tax had been upheld merely as a supplementary corporate income tax, it concluded on remand in the *Penney* case that even under the construction of the law as a tax on the stockholder,—“\* \* \* we are bound by its decision \* \* \*”. (*J. C. Penney Co. vs. Tax Commission*, 238 Wis. 69, 74.). The assumption made by the Supreme Court of the State of Wisconsin that even though the construction placed upon the law by that Court was different than the construction placed upon the law by this Court, that the decision in this Court nevertheless controlled on the constitutional question of jurisdiction was further emphasized in the opinion of Mr. Justice Wickhem in the *Wisconsin Gas and Electric Co. vs. Department of Taxation*, 243 Wis. 216 at 220 where it is said:

“At this stage of the litigation we are not concerned with the question of the power to tax and we must assume that the power vindicated is the power to levy the tax that was before the United States supreme court for consideration.”

The error of the Wisconsin Supreme Court which gives rise to this appeal on the constitutional question of jurisdiction, was in not realizing that since it was unable to adopt the construction upon which this Court held the law to be valid, it must proceed to an independent consideration of constitutionality on the basis of such construction of the Act as finally adopted.

**Point II:** As a privilege tax against the stockholder the law is clearly unconstitutional under the Fourteenth Amendment of the Constitution of the United States as taking the property of appellant and its stockholders without due process of law.

As indicated in the statement of the case, appellant is a Delaware corporation, with its principal office in St. Paul, Minnesota. Directors meetings are held at St. Paul and the dividends involved in this litigation have been declared there. Only a small percentage of its stockholders reside within Wisconsin. If this Court is to sustain the law as now interpreted against the stockholders of a foreign corporation, it must now hold that Wisconsin has the power to exact a tax from *nonresident stockholders of a foreign corporation* merely because some part of the dividend was *earned by the corporation in Wisconsin*. If Wisconsin may not constitutionally directly impose its income tax upon income payable to nonresident stockholders of a foreign corporation, it would appear to be *a fortiori* clearly unconstitutional for it to impose a tax upon such stockholders at the time of a payment of a dividend to the stockholders which corporation is required to deduct.

The privilege of *earning* income in the State of Wisconsin by the corporation is *entirely separate and distinct from the privilege of receiving a dividend out of income* in the surplus account. The privilege of earning the income of the corporation in Wisconsin is a privilege granted to the corporation by Wisconsin that can be taxed and has been taxed against the corporation under the general income tax laws. The privilege of paying and receiving the dividend earned in Wisconsin in prior years to stockholders of a foreign corporation is a privilege neither conferred nor controlled by Wisconsin and may not be taxed by it.

During the entire course of this litigation there has been no suggestion that the Privilege Dividend Act, as a tax on nonresident stockholders, would be constitutional. The difference between the majority and minority opinions of this Court in the *J. C. Penney* case was not as to whether the tax would be constitutional as one on nonresident stockholders, but rather whether, without judicial legislation, the tax could be upheld by considering it as a supplementary corporate income tax. The majority of this Court held merely that the tax in question was valid as a supplementary corporate income tax, both because in its measure and its assumed incidence it had relation to transactions within Wisconsin. This Court did not alter the rule that the measure and incidence of the tax must be related to transactions within the taxing state. A supplementary income tax measured by Wisconsin income, and having its incidence upon the corporation to which the State had granted the privilege of doing business within its borders, would probably fit into the permissible scope of state taxing power. This is not true of a tax upon the right of a nonresident stockholder to receive dividends, since such right is enjoyed under the laws of a sister state and is not exercised within the limits of Wisconsin. Since the majority of appellant's stockholders are nonresidents, the tax as now construed is placed on a foreign subject matter (dividends received by stockholders) and depends upon a foreign contingency (declaration of dividends outside of Wisconsin).

In the *J. C. Penney* case this Court distinguished its prior decision in *Connecticut General Life Insurance Company vs. Johnson*, 303 U. S. 77, by stating that as a supplementary income tax, "the incidence of the tax, as well as its measure, is tied to the earnings which the State of Wisconsin has made possible \* \* \*". The *Connecticut General Life Insurance Company* case involved an attempt by Cali-

ifornia to tax re-insurance contracts made in Connecticut by a Connecticut corporation on policies issued to California residents. At page 80 this Court said:

"But the limits of the state's legislative jurisdiction to tax, prescribed by the Fourteenth Amendment, are to be ascertained by reference to the incidence of the tax upon its objects rather than the ultimate thrust of the economic benefits and burdens of transactions within the state. As a matter of convenience and certainty, and to secure a practically just operation of the constitutional prohibition, we look to the state power to control the objects of the tax as marking the boundaries of the power to lay it. Hence it is that a state which controls the property and activities within its boundaries of a foreign corporation admitted to do business there may tax them. But the due process clause denies to the state power to tax or regulate the corporation's property and activities elsewhere. (Citing) It follows that such a tax, otherwise unconstitutional, is not converted into a valid exaction merely because the corporation enjoys outside the state economic benefits from transactions within it, which the state might but does not tax, or because the state might tax the transactions which the corporation carries on outside the state if it were induced to carry them on within."

As this Court stated:

" \* \* \* we look to the state power to control the objects of the tax as marking the boundaries of the power to lay it."

Wisconsin does not acquire jurisdiction to tax dividends of nonresident stockholders " \* \* \* merely because the corporation enjoys outside the state economic benefits from transactions within it \* \* \* ". Wisconsin confers no privilege in connection with the receipt of such dividends by the stockholder.

In *Provident Savings Life Assurance Society vs. Kentucky*, 239 U. S. 103, the United States Supreme Court considered a Kentucky privilege tax on a life insurance company formerly doing business in Kentucky but which had withdrawn from the state. The premiums were paid to the company's New York office. The Court held that Kentucky could not lay a privilege tax on the business. At page 111 this Court stated:

"Taxation without jurisdiction has been held to be a violation of the Fourteenth Amendment (*Louisville & J. F. Co. vs. Kentucky*, 188 U. S. 385; *Delaware L. & W. R. Co. vs. Penn.*, 198 U. S. 341; *Union Ref. Transit Co. vs. Kentucky*, 199 U. S. 194); and the principle involved applied to the assertion of authority on the part of the state to exact a license tax for the privilege of doing acts which lie beyond the sphere of local control."

See also:

*St. Louis Compress Co. vs. Arkansas*, 260 U. S. 346, 348, 349;

*Louisville etc. Ferry Co. vs. Kentucky*, 188 U. S. 385, 396;

*Union Refrigerator Transit Co. vs. Kentucky*, 199 U. S. 194, 202;

*State Tax on Foreign Held Bonds*, 15 Wall. 300, 319.

Jurisdiction of the state to levy an income tax upon the income of nonresidents derived from sources within the state is well settled, but the state does not derive its right to levy the tax from the fact that the payor of income is within the state. Jurisdiction over nonresident stockholders does not exist here, and jurisdiction over the subject matter of the transfer would exist if at all only by dis-regarding the corporate entity.

If it is contended that the jurisdictional justification of the tax is because Wisconsin gave protection to the earning of the income found in the dividend; it is of course self-evident that the protection was given to the *corporation*, not to the stockholder. If it is said that the tax can be justified against the stockholder, as a legitimate "charge" for the doing of corporate business within Wisconsin by the corporation, it can only be done by an utter, complete and unwarranted disregard of the corporate entity. The alleged protection and benefits which Wisconsin gave were of course granted to the corporation,—but the tax is on the stockholder. And the obvious should here be observed,—that the general income tax under the laws of Wisconsin has been imposed upon the corporation based upon the conception of the appellant as a separate entity, the corporate income of the appellant having properly been subjected to the income tax laws of Wisconsin. By the privilege dividend tax law as now construed, this same income is sought to be taxed against a foreign stockholder on the receipt of the same in the form of dividends. We reiterate that as a tax upon the stockholder, the law can be sustained only by complete and utter disregard of the corporate entity.

The Wisconsin Supreme Court in its assumption that this Court had sustained the constitutionality of the law, regardless of its proper construction,—recognized that to some extent the corporate entity has been disregarded. (*Wisconsin Gas and Electric Co. vs. Department of Taxation*, 243 Wis. 216, 220.)

There is no justifiable basis whatsoever for the disregard of the corporate entity in the instant case. The security of business transaction, the regard of the common law for the corporate entity where its existence is used legitimately, is entitled to protection and should be protected.

This Court only recently in an opinion by Mr. Justice Reed in *Moline Properties, Inc. vs. Commissioner of Internal Revenue*, 319 U. S. 436, 438, had occasion to consider the conception of corporate entity and its relation to other phases of the law and particularly to tax law. It was specifically recognized and assumed, as well it necessarily should have been, that the corporate entity where legitimately used, has recognized usefulness in business life and should not be disregarded.

It is of course fundamental, as summarily reflected in Vol. 1, *Fletcher's Encyclopedia of Law of Private Corporations*, Permanent Edition, Sections 24-48, that the corporate entity will normally be respected. Section 40 supports the proposition:

“ . . . Corporate property and stockholder's property and themselves are distinct for purposes of taxation ”.

It is further of course fundamental, that the corporate entity may be disregarded where necessary to defeat fraud, avoid contravention of law or promote justice. But this rule is only applied under special circumstances.

(cf. *Anderson vs. Abbott et al*, United States Supreme Court, October Term, 1943, No. 3, decided March 6, 1944, 12—U. S. Law Week, 4211 at 4213.)

The following are the more recent pronouncements by this Court in support of the rule that the corporate entity may be disregarded *only under special and peculiar circumstances*:

*Burnett vs. Commonwealth Improvement Co.*  
(1932) 287 U. S. 415, 77 L. Ed. 399;

*New Colonial Ice Company vs. Helvering*, (1934)  
292 U. S. 435, 78 L. Ed. 1348;

See also *Page et al vs. Haverty*, (1942) 129 Fed. 2d 512;

And for an extended citation of earlier authority, see *Majestic Co. vs. Orpheum Circuit, Inc.*, (1927) 21 Fed. 2d 720.

In the *New Colonial Ice Co.* case the Court says:

"As a general rule a corporation and its stockholders are deemed separate entities and this is true in respect of tax problems. Of course, the rule is subject to the qualifications that the separate identity may be disregarded in exceptional situations where it otherwise would present an obstacle to the due protection or enforcement of public or private rights."

[The Wisconsin Court has steadfastly recognized the corporate entity in tax matters. (cf. *Estate of Shephard*, 184 Wis. 88, 94).]

No principles of justice require the disregard of the corporate entity in order to sustain the dividend tax. Wisconsin has the power to tax and is now taxing the income of the corporation earned in Wisconsin and the property of the corporation located in Wisconsin. It has the power to increase these taxes. To deny it the right to tax foreign stockholders will in no way deprive it of a power to raise revenue, but will only limit the exercise of that power to proper objects of taxation. On the other hand, there are numerous principles of justice which operate to compel the respect for the corporate entity.

Under the federal system, the taxing power is exercised continuously by over fifty separate jurisdictions, and their various subdivisions. This Court has repeatedly stated in recent years that problems of taxation are "eminently practical" in nature and should be dealt with in that spirit by the Courts. There are many "practical" reasons why the corporate entity should not be disregarded. The tax obvi-

ously disturbs the contractual relationship between the corporation and any class of stockholders which by contract may be entitled to preferential treatment. The necessity of computing and reporting the tax, deducting the tax from every dividend paid to every stockholder, and advising the stockholder with respect to each deduction creates excessive and unreasonable burdens upon the corporation. If this tax is sustained, this Court thereby encourages competition among the states in seeking revenue from sources beyond their respective borders. The indirect means adopted by the state to retax income which has already been subjected to the Wisconsin tax is an inappropriate exercise of the state's power particularly in view of its right to tax the income of the corporation directly, or to increase that tax by merely increasing corporate rates.

Unless the corporate entity is entirely disregarded, the attempt of Wisconsin to tax a stockholder of a foreign corporation not resident in Wisconsin, is an attempt to "charge" such stockholder for something it has not given him. This is beyond the taxing jurisdiction of Wisconsin. As Mr. Justice Frankfurter stated in the concurring opinion rendered in *State Tax Commission vs. Aldrich*, 316 U. S. 174, at 182:

"Of course, the Due Process Clause has its application to the taxing powers of the States—a State cannot tax a stranger for something it has not given him. When a state gives nothing in return for exacting a tax, it may be said that there is no 'jurisdiction to tax'".

The stockholder is a "stranger" to the privilege that Wisconsin gave the corporation in earning the income.

The Wisconsin Supreme Court has now adopted the same construction of the privilege dividend tax as was originally advanced in the dissenting opinion of this Court. The

appellant, therefore, respectfully submits that the rationale of the dissenting opinion be accepted as controlling this case. As Mr. Justice Roberts stated at page 448 of 311 U. S.:

"By the very terms of the Act, the tax is laid not on the corporation but on the stockholder receiving the dividend, and, by confession, thousands of such stockholders are not residents of Wisconsin. The corporation is the mere collector of the tax and the penalty for failure to collect it is that the corporation must pay it. If the exaction is an income tax in any sense it is such upon the stockholder and is obviously bad."

And as stated at 449:

"If Wisconsin found that dividend income of stockholders of domestic corporations escaped taxation and should bear it, an effective way to reach the dividend receipts of the stockholder of such corporations was to place a tax upon the receipts of dividend by them. But such a levy upon the stockholders of a foreign corporation, not resident in Wisconsin, obviously was impossible, although that is exactly what was attempted by the statute in question."

Viewed as a privilege tax on the stockholder, there clearly is not a sufficient "nexus" between the earning of the income by the corporation in Wisconsin,—and the subsequent receipt of a dividend from a foreign corporation by a foreign stockholder on which to predicate jurisdiction to tax.

**Point III:** The tax as computed by the State is unconstitutional retroactive.

Even admitting for the purpose of argument that jurisdiction exists to impose some tax, it is self-apparent that the method adopted by the Department of Taxation resulted in subjecting alleged Wisconsin income in surplus to a tax by a law passed years after that income was earned

and transferred to surplus. The assessment as made by the Department is clearly vulnerably retroactive.

As previously stated, the Department in making the computation involved herein analyzed the surplus account of Minnesota Mining & Manufacturing Co. from the date it began business in Wisconsin to December 31st of the year preceding the year in which a dividend was declared in an effort to ascertain what portion of the surplus might be attributable to income derived from Wisconsin business. Proceeding in this manner, the Department year by year determined the ratable contributions of earnings within and without Wisconsin to surplus from the commencement of business in the state, up to December 31st prior to the date of the declaration of the dividend. The Department then took the Wisconsin income in said surplus as the numerator and the total surplus as the denominator of a fraction deemed to be representative of the portion of Wisconsin income in surplus. This fraction was reduced to a percentage and applied to dividends as periodically declared in the following year. The result was claimed to be the amount of Wisconsin income that was distributed by such dividends.

While there is no express statutory authorization for this formula, and there appeared to be no clear indication of what formula the Legislature would have adopted if it chose to act, the Supreme Court of Wisconsin nevertheless construed the law to reflect the intention of the Legislature to tax such accumulations of Wisconsin income in the surplus of foreign corporations *regardless of when earned*.

*(International Harvester Company vs. Department of Taxation, 243 Wis. 198, 206.)*

The only jurisdictional basis ever urged to support the law and tax, so far as it involved dividends of a foreign corporation, was that Wisconsin gave protection to the

earning of the income. If the jurisdictional question is "whether the state has given anything for which it can ask a return" (*Wisconsin vs. J. C. Penney Co.*, *supra*, page 444),—and if this Court wholly disregards the corporate entity and determines that the stockholders also can be "charged" for the protection given to the corporation in the earning of the income used in the payment of a dividend,—the indisputable salient fact remains that this protection was given only in the year in which the income was earned,—not at such later time as such income might be used in the transaction of a dividend. The formula used by the Wisconsin Department of Taxation imposes a tax for a privilege admittedly granted years before the enactment of the law so taxing it. The decisions are conclusive to the effect that while retroactive income taxes are permissible, they cannot be imposed without limit and are upheld only as to recent transactions.

*Welch vs. Henry*, 305 U. S. 134, affirming 236 Wis. 595;

*People ex rel vs. Beck et al vs. Graves*, 280 N. Y. 405, 21 N. E. (2d) 371 at 372 where the case of *Welch vs. Henry*, 305 U. S. 134, is discussed.

See also with respect to constitutional problem of retroactive excise taxes:

*Nichols vs. Coolidge*, 274 U. S. 531, 542, 543;

*Blodgett vs. Holden*, 275 U. S. 142, 147;

*Untermeyer vs. Anderson*, 276 U. S. 440, 445;

*Coolidge vs. Long*, 282 U. S. 582, 595, 596;

cf. *Cooper vs. U. S.*, 280 U. S. 409.

For one of the most recent discussions of the constitutionality of retroactive excise taxes, see:

*Matter of Lacadin Realty Corp. vs. Graves*, 288 N. Y. 354.

There is also a definite indication in the cases treating the constitutionality of retroactive taxes that the matter of "anticipation" of the possibility of the enactment of the particular tax law may be important. We submit that the enactment of the privilege dividend tax law by Wisconsin in 1935 could not have been reasonably anticipated by any potential taxpayer prior to the time that the legislation was initiated. There was clearly no adequate "forewarning" that such a tax would be enacted, or precedent for the Wisconsin privilege dividend tax under the tax pattern adopted by the State of Wisconsin. Indeed so far as we are aware, neither was there any precedent for the type of law in question under the laws of any other state. Accordingly, there is no basis to contend in an argument to save the law from unconstitutional retroactivity that the taxpayer might reasonably have anticipated the enactment of the law and the imposition of the tax in question.

It is further perfectly obvious that the stockholders of a particular corporation may be quite different, or indeed entirely different, at the time that a dividend is paid, from those existing years before at the time the income of the corporation, which may be used in the dividend, was earned. We thus have the anomalous situation, if the tax is sustained, of a taxpayer (the stockholder) paying for the privilege given to the corporation in earning the income years before the stockholder acquired stock in the corporation.

Another observation should here be made of the retroactivity features of the law. It has been argued by the opposition that the tax is merely measured by accrued income that has not been previously distributed and still remains income,—and that the tax attaches when there is a distribution thereof as income. But the argument requires the conclusion that "once income always income",—and if

carried to its logical conclusion would require the designation of most property as income because it was originally derived from income. There of course must be some time limit when accumulated income in surplus loses its identity as income for tax purposes.

cf. *Appeal of Siesel*, 217 Wis. 661, 665;

*Fitch vs. Tax Commission*, 201 Wis. 383, 391;

*State ex rel Sally F. Moon Co. vs. Tax Commission*, 166 Wis. 287, 293;

See also article by Arthur Leon Harding, "State Jurisdiction to Tax Dividends and Stock Profits to Natural Persons", 25 *California Law Review*, 139, 158.

The suggestion has been made that the tax is not retroactive if it is viewed as a transaction tax in view of the fact that the transaction takes place after the enactment of the law. We submit however that the formula as applied is equally vulnerable because in fact income is being taxed under the guise of a tax upon the privilege of distributing it. If the only jurisdictional justification of the tax is that it relates to income earned by the corporation in Wisconsin, and if income earned more than a year or two before the enactment of a tax law is exempt from tax, such exemption should not be circumvented by imposing the tax *nominally* upon the transaction instead of on the income, which is the subject matter of the transaction. Validity cannot be given to an invalid retroactive tax upon accumulated Wisconsin income by making it contingent upon a contemporary foreign event. As this Court said in the *J. C. Penney* case, the description of the tax is of no moment in determining the constitutional significance of the exaction and the tax as computed is not rendered less retroactive by giving it a different label.

The Wisconsin Court was evenly divided on the constitutionality of this alleged retroactive application of the tax. By reason of the fact that the lower court had ruled in favor of constitutionality, the taxpayer's contention that the law was unconstitutional was denied. Our views concerning the unconstitutional retroactivity of the tax are well expressed by Mr. Justice Wickhem in the *International Harvester Company* case, 243 Wis. 198, where he stated at page 208:

"Mr. Chief Justice *Rosenberry*, Mr. Justice *Martin*, and the writer are of the view, (1) that since the United States supreme court has held that the label placed upon this law by the legislature or by this court is wholly ineffective to impair its constitutionality as against the contention that Wisconsin is without power to levy the tax, such label or designation or the selection by Wisconsin of the payment and receipt of the dividend as the occasion for the tax is equally ineffective to save it from objections to its retroactivity; (2) that the earnings of the corporation in Wisconsin upon which are grounded Wisconsin's power to levy the dividend tax must be within reach of a retroactive tax; (3) that the extent of permissible retroactivity should be determined upon the analogy of the income tax cases; (4) that retroactivity should only be permitted to 'recent' transactions; (5) that consistently with these principles the tax may not be applied to earnings in Wisconsin which accrued prior to the last corporate fiscal year preceding the enactment of Wisconsin privilege dividend tax; (6) that by reason of the severability clause, the operation of the tax should be so limited; (7) that nothing in the decision upon remand requires a different conclusion."

We thus submit that even if this Court should determine, by disregarding the corporate entity, that Wisconsin had jurisdiction to impose *some* tax, that to permit of the imposition of a tax on Wisconsin earnings in surplus, earned

years before the enactment of the law, is so harsh, arbitrary and oppressive as to transgress constitutional limits.

### Conclusion.

It is respectfully submitted that the law as a privilege tax upon stockholders of foreign corporations is clearly unconstitutional under the Fourteenth Amendment of the United States, and that the judgment of the Supreme Court of the State of Wisconsin to the contrary should be reversed.

It is further respectfully submitted in the alternative that in any event so much of the law as attempts to tax alleged Wisconsin income in surplus, *regardless of when earned*, is unconstitutional under the Fourteenth Amendment of the United States of America.

Respectfully submitted,

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**Appendix.**

The statutes and laws of the State of Wisconsin which are involved, are as follows: Section 3, Chapter 505, Laws of Wisconsin, 1935, effective on its publication on September 26, 1935, and as amended by Chapter 552, Laws of Wisconsin, 1935, effective on its publication on October 8, 1935, provide:

“Section 3. *Privilege Dividend Tax.* (1) For the privilege of declaring and receiving dividends, out of income derived from property located and business transacted in this state, there is hereby imposed a tax equal to two and one-half per centum of the amount of such dividends declared and paid by all corporations (foreign and local) after the passage and publication of this act and prior to July 1, 1937. Such tax shall be deducted and withheld from such dividends payable to residents and nonresidents by the payor corporation.

(2) Every corporation required to deduct and withhold any tax under this section shall, on or before the last day of the month following the payment of the dividend, make return thereof and pay the tax to the tax commission, reporting such tax on the forms to be prescribed by the tax commission.

(3) Every such corporation hereby made liable for such tax, shall deduct the amount of such tax from the dividends so declared.

(4) In the case of corporations doing business within and without the state of Wisconsin, such tax shall apply only to dividends declared and paid out of income derived from business transacted and property located within the state of Wisconsin. The amount of income attributable to this state shall be computed in accordance with the provisions of chapter 71. In the absence of proof to the contrary such dividends shall be presumed to have been paid out of earnings of such corporation attributable to Wisconsin under the provisions of chapter 71, for the year

immediately preceding the payment of such dividend. If a corporation had a loss for the year prior to the payment of the dividend, the tax commission shall upon application, determine the portion of such dividend paid out of corporate surplus and undivided profits derived from business transacted and property located within the state.

(5) Dividends paid by a subsidiary corporation to its parent shall not be subject to the tax herein imposed provided that the subsidiary and its parent report their income for taxation under the provisions of chapter 71 on a consolidated income return basis, or both corporations report separately.

(6) The provisions of this section shall not apply to dividends declared and paid by a Wisconsin corporation out of its income which it has reported for taxation under the provisions of chapter 71, to the extent that the business of such corporation consists in the receipt of dividends from which a privilege dividend tax has been deducted, and withheld and the distribution thereof to its stockholders.

(7) For the purposes of this section dividends shall be defined as in section 71.02, except that the tax herein imposed shall not apply to stock dividends or liquidating dividends.

(8) The tax hereby levied, if not paid within the time herein provided, shall become delinquent and when delinquent shall be subject to a penalty of two per cent on the amount of the tax and interest at the rate of one-half per cent per month until paid.

(9) The tax hereby imposed shall, when collected by the tax commission, be paid by it into the state treasury."

The above legislation was extended in operation by Chapter 309 of the Session Laws of Wisconsin of 1937 to July 1st, 1939, and by Chapter 198 of the Session Laws of 1939 to July 1st, 1941, further by Chapter 198 of the Session Laws of 1939, the rate was increased from two and

one-half per cent ( $2\frac{1}{2}\%$ ) to three per cent (3%). Chapter 223, Session Laws of 1937, also slightly amended the law, but such amendment has no bearing on the controversy here involved.